

(3) "Customer" means an individual who obtains from a bank an extension of credit that is primarily for personal, family, or household purposes. For purposes of this subchapter, the term means the same thing as "borrower."

(4) "Debt cancellation contract" means a loan term or contractual arrangement modifying loan terms under which a bank agrees, for a fee, to cancel all or part of a customer's obligation to repay an extension of credit from that bank upon the occurrence of a specified event. The agreement must specify the extension of credit to which it pertains. The agreement may be separate from or a part of other loan documents. A debt cancellation contract may be offered and purchased either contemporaneously with the other terms of the loan agreement or subsequently.

(5) "Debt suspension agreement" means a loan term or contractual arrangement modifying loan terms under which a bank agrees, for a fee, to suspend all or part of a customer's obligation to repay an extension of credit from that bank upon the occurrence of a specified event. The agreement must specify the extension of credit to which it pertains. The agreement may be separate from or a part of other loan documents. The term "debt suspension agreement" does not include loan payment deferral arrangements in which the triggering event is the borrower's unilateral election to defer repayment or the bank's unilateral decision to allow a deferral of repayment.

(6) "Guaranteed asset protection (GAP) waiver or agreement" means an extension of credit or contractual arrangement modifying terms of an extension of credit for the purchase of titled personal property under which a bank agrees to cancel the customer's obligation to repay the portion of the extension of credit that exceeds the amount paid by the primary insurer of the titled personal property upon the insurer's declaration that the titled personal property is a total loss or determination that the titled personal property is stolen and not recoverable.

(7) "Loan or extension of credit" means a direct or indirect advance of funds to a customer made on the basis of any obligation of that customer to repay the funds or that is repayable from specific property pledged by or on the customer's behalf. The term also includes any liability of a bank to advance funds to or on behalf of any customer pursuant to a contractual commitment.

(8) "Residential mortgage loan" means a loan for personal, family, or household purposes secured by a one- to four-family residential property.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: Definitions of the terms in sections (1), (2), (3), (4), (5), and (8) are substantially equivalent to the definitions of the same terms in 12 CFR 37.2. The department has determined that the federal definitions will be sufficient to serve the department's purposes and meet the Legislature's intent. Because these definitions already exist, the department saw no need to write its own original definitions.

The definition of "guaranteed asset protection (GAP) waiver or agreement" in (6) is substantially equivalent to and adapted from Office of the Comptroller of the Currency (OCC) Interpretive Letters #1028 and #1032 concerning GAP waivers or

agreements as they relate to debt cancellation contracts. The department believes the OCC's description of GAP waivers or agreements in the interpretive letters is clear and that the definition adapted from the letters is sufficient to serve the department's purposes and meet the Legislature's intent.

The definition of "loan or extension of credit" in (7) is substantially equivalent to and adapted from 12 USC 84(b)(1). The definition was selected because it encompasses both advanced funds and commitments to advance funds such as letters of credit. The department chose to define "loan or extension of credit" for clarification purposes because the term is used throughout 12 CFR Part 37 upon which these rules are patterned, but the term is not defined in that part.

NEW RULE II DEBT CANCELLATION AND DEBT SUSPENSION PROGRAMS – REQUIREMENTS (1) A bank offering debt cancellation contracts and/or debt suspension agreements shall:

(a) manage the risks associated with debt cancellation contracts and debt suspension agreements in accordance with bank safety and soundness principles by establishing and maintaining effective risk management and control processes over its debt cancellation contracts and debt suspension agreements to include:

(i) appropriate recognition and financial reporting of income, expenses, assets, and liabilities;

(ii) appropriate treatment of all expected and unexpected losses associated with the contracts; and

(iii) assessment of the adequacy of its internal control and risk mitigation activities in view of the nature and scope of the bank's debt cancellation and debt suspension program; and

(b) obtain and maintain in effect insurance approved by the State Auditor and Commissioner of Insurance to cover all of the bank's risk associated with its debt cancellation contracts and debt suspension agreements.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: Subsection (1)(a) is substantially equivalent to 12 CFR 37.8. The department has determined that the federal regulation, together with subsection (1)(b), will be sufficient to serve the department's purposes and meet the Legislature's intent.

Subsection (1)(b) adds a requirement that has no counterpart or equivalent in the federal regulations making this rule more stringent than 12 CFR 37.8. National banks are permitted but not required to manage the risk associated with their debt cancellation contracts and debt suspension agreements by obtaining insurance coverage. The department believes the best practice, consistent with bank safety and soundness principles, is to require insurance coverage. The potential losses that a bank is exposed to when it offers debt cancellation contracts and debt suspension agreements could be significant. Ideally, a bank could maintain a robust and effective internal program of monitoring and managing the risk without insurance, but that ideal may not always be met. A bank may not fully appreciate the extent of its risk exposure at all times if, for example, it does not retain an

actuarial consultant. The department believes this reality poses an unacceptable risk to the bank's safety and soundness.

Bank service organizations and other vendors offer services to banks related to administration of the banks' debt cancellation and debt suspension programs. The service organizations' and vendors' products include an insurance component that was cited by the industry and by vendors in their discussions with the department regarding HB 432 prior to its passage. The insurance component was an important consideration of the department in its decision not to oppose the bill. The department does not believe that requiring a bank to obtain insurance coverage for its risks associated with offering debt cancellation contracts, for example, changes the essential character of the two-party debt cancellation contract or converts it to an insurance product.

Under HB 432, debt cancellation contracts and debt suspension agreements between customers and banks under which there is no obligation on the part of a third-party insurer to pay the customer's loan balance or make loan payments on behalf of the customer upon the occurrence of the identified event are not insurance. By contrast, under an insurance contract between a bank and an insurer covering the bank's risks associated with offering debt cancellation contracts, for example, the insurer is obligated to pay the bank for the loss it sustains when a debt cancellation contract is activated by the occurrence of the identified event. Clearly, the latter transaction is an insurance transaction that is subject to the provisions of Title 33, MCA.

NEW RULE III REQUIRED DISCLOSURES (1) A bank shall provide the following disclosures to the bank's customer at the time of offering the customer a debt cancellation contract or debt suspension agreement:

- (a) notice of the prohibited acts or practices contained in [NEW RULE IV];
- (b) the fee applicable to the contract and any payment options;
- (c) any refund policy if the fee is paid in a single payment and added to the amount borrowed;
- (d) whether the customer is barred from using the credit line to which it pertains if the debt cancellation contract or debt suspension agreement is activated;
- (e) eligibility requirements, conditions, and exclusions;
- (f) that a debt suspension agreement, if activated, does not cancel the debt, but only suspends payment requirements; and
- (g) notice that cancellation of debt may result in a tax liability to the customer if activated.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: Subsections (1)(b) through (1)(f) are substantially equivalent to 12 CFR 37.6. The department has determined that the federal regulation, when combined with subsections (1)(a) and (1)(g) of this rule, provides sufficient information to enable a bank customer to make an informed decision concerning the purchase of a debt cancellation contract or debt suspension agreement.

Subsection (1)(a) requires a bank to give the customer notice of what acts or practices of a bank pertaining to debt cancellation contracts and debt suspension agreements are prohibited under New Rule IV. The department believes that customers with knowledge of the prohibited acts and practices can more effectively assert the protections that the law affords them. Subsection (1)(a) may also protect banks from unfounded customer claims that the customer was unaware of relevant information or was misled.

Subsection (1)(g) has no equivalent or counterpart in the federal regulation pertaining to debt cancellation contracts and debt suspension agreements. During the hearings on HB 432, Sen. Balyeat asked the bill proponents whether activation of a debt cancellation contract was a taxable event. While subsection (1)(g) does not require a bank to give its customer tax advice on Internal Revenue Code §6050P or any other provisions of the tax code, it requires that the customer be given notice of the potential tax liability if a debt cancellation contract is activated. The requirement in (1)(g) makes this rule more stringent than 12 CFR 37.6. The department believes that, given Sen. Balyeat's comment, it is important that the customer know of a potential tax liability.

NEW RULE IV PROHIBITED ACTS OR PRACTICES (1) A bank is prohibited from engaging in any of the following acts or practices:

- (a) extending credit or altering the terms or conditions of an extension of credit conditioned upon the customer entering into a debt cancellation agreement or debt suspension agreement with the bank. The prohibition is commonly referred in the regulatory context as the anti-tying provision;
- (b) engaging in any practice or using any advertisement that could mislead or otherwise cause a reasonable person to reach an erroneous belief with respect to information that must be disclosed under [NEW RULE III], including what is being offered, the cost, and/or the terms of the contract;
- (c) offering debt cancellation contracts or debt suspension agreements that contain terms:
 - (i) giving the bank the right unilaterally to modify the contract unless:
 - (A) the modification is favorable to the customer and is made without additional charge to the customer; or
 - (B) the customer is notified of any proposed change and is provided a reasonable opportunity to cancel the contract without penalty before the change goes into effect; or
 - (ii) requiring an up-front, lump-sum single payment for the contract if the extension of credit to which the contract pertains is a residential mortgage loan.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: This rule is substantially equivalent to 12 CFR 37.3. The department believes that the federal regulation will serve the department's purposes and meet the Legislature's intent. This rule adds examples of the areas in which a customer could be misled or come to an erroneous belief as a result of a bank's practices or advertising. The examples were cited in a

recent case in which a federal regulator imposed large civil penalties against a national bank related to its marketing of credit protection products. The department believes that inclusion of specific examples in (1)(b) provides more clarity to the rule.

NEW RULE V REFUNDS OF FEES UPON TERMINATION OR PREPAYMENT OF COVERED LOAN (1) If a debt cancellation contract or debt suspension agreement is terminated, including, for example, when the customer prepays the covered loan, a bank shall refund to the customer any unearned fees paid for the contract unless the contract provides otherwise.

(2) A bank may offer a customer a contract that does not provide for a refund only if the bank also offers that customer a bona fide option to purchase a comparable contract that provides for a refund.

(3) A bank shall calculate the amount of a refund using a method at least as favorable to the customer as the actuarial method.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: This rule is substantially equivalent to 12 CFR 37.4. The department believes that the federal regulation will be sufficient to serve the department's purposes, meet the Legislature's intent, and ensure fairness to a bank's customer by providing refund options as well as overall clarity to the refund issue.

NEW RULE VI METHOD OF PAYMENT OF FEES (1) Except as provided in [NEW RULE IV(1)(c)(ii)], a bank may offer a customer the option of paying the fee for a debt cancellation contract or a debt suspension agreement in a single payment, provided the bank also offers the customer a bona fide option of paying the fee for that contract in periodic installment payments.

(2) If a bank offers the customer the option to finance the single payment by adding it to the loan principal, the bank must also disclose, in accordance with [NEW RULE V], whether the customer may cancel the agreement and receive a refund, and, if so, the time period during which the customer may do so.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: This rule is substantially equivalent to 12 CFR 37.5. The department believes that the federal regulation will be sufficient to serve the department's purposes, meet the Legislature's intent, and, together with NEW RULE V, provide overall clarity to the refund issue.

NEW RULE VII AFFIRMATIVE ELECTION TO PURCHASE AND ACKNOWLEDGMENT OF RECEIPT OF DISCLOSURES (1) Before entering into a debt cancellation contract or debt suspension agreement, a bank shall obtain the customer's written affirmative election to purchase the contract and a written acknowledgment of receipt of the disclosures required under [NEW RULE III].

(2) The election and acknowledgment information must be conspicuous, simple, direct, readily understandable, and designed to call attention to its significance.

(3) The election and acknowledgment information satisfies these standards if it conforms to the following requirements:

(a) if the sale of a contract occurs by telephone, the customer's affirmative election to purchase may be made orally, provided that the bank:

(i) maintains sufficient documentation to show that the customer received the short-form disclosures substantially similar to [NEW RULE VIII(1)] and then affirmatively elected to purchase the contract;

(ii) mails to the customer the affirmative written election and written acknowledgment together with a long-form disclosure substantially similar to [NEW RULE VIII(2)], within three business days after the telephone solicitation, and maintains sufficient documentation to show it made reasonable efforts to obtain the documents from the customer; and

(iii) permits the customer to cancel the purchase of the contract without penalty within 30 days after the bank has mailed the long-form disclosures to the customer.

(b) if the contract is solicited through written materials such as mail inserts or "take one" applications and a bank provides only the short-form disclosures in the written materials, then the bank shall mail the acknowledgment of receipt of disclosures, together with a long-form disclosure as provided under [NEW RULE VIII(2)], to the customer within three business days, beginning on the first business day after the customer contacts the bank or otherwise responds to the solicitation. A bank may not obligate the customer to pay for the contract until after the bank has received the customer's written acknowledgment of receipt of disclosures unless the bank:

(i) maintains sufficient documentation to show that the bank provided the acknowledgment of receipt of disclosures to the customer;

(ii) maintains sufficient documentation to show that the bank made reasonable efforts to obtain from the customer a written acknowledgment of receipt of the long-form disclosures; and

(iii) permits the customer to cancel the purchase of the contract without penalty within 30 days after the bank has mailed the long-form disclosures to the customer.

(4) The affirmative election and acknowledgment may be made electronically in a manner consistent with the requirements of the Electronic Signatures in Global and National Commerce Act, 15 USC 7001 et seq. and the Uniform Electronic Transaction Act, Title 30, chapter 18, part 1, MCA.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: This rule is substantially equivalent to 12 CFR 37.7. The department believes that the federal regulation is sufficient to serve the department's purposes, meet the Legislature's intent, and protect both the bank and its customer. Subsection (3)(c) includes a citation to state

law relating to electronic transactions that is not included in 12 CFR 37.7. The addition of the reference to state law will clarify for banks that a customer's affirmative election and acknowledgment pertaining to the purchase of a debt cancellation or debt suspension contract may be in electronic form.

NEW RULE VIII DISCLOSURE FORMS (1) The department adopts as a model, but not as a requirement, the Comptroller of the Currency's model short form disclosure at 12 CFR 37 App A revised as of January 1, 2010. The form must be adapted by the bank to include the disclosures required under [NEW RULE III(1)(a) and (g)].

(2) The department adopts as a model, but not as a requirement, the Comptroller of the Currency's model long-form disclosure at 12 CFR 37 App B revised as of January 1, 2010. The form must be adapted by the bank to include the disclosures required under [NEW RULE III(1)(a) and (g)].

(3) The model forms in (1) and (2), which are available at Title 12, Volume I, Part 37, Appendices A and B in the Code of Federal Regulations, are not mandatory, but a bank that provides disclosures in a form substantially similar to the adapted model forms will be deemed to have satisfied the disclosure requirements applicable to the bank concerning its debt cancellation and/or debt suspension program.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: This rule is substantially equivalent to 12 CFR Part 37, Appendices A and B, except this rule requires a bank to adapt the federal forms to include the requirements imposed by these rules that have no counterpart or equivalent in federal regulations so that the disclosures are consistent with these rules.

NEW RULE IX GUARANTEED ASSET PROTECTION (GAP) FEATURE

(1) A debt cancellation contract with a GAP feature offered in connection with an extension of credit for the purchase of titled personal property for personal, family, or household use is a single product and does not require a separate agreement related to financing for the GAP feature. A bank offering a debt cancellation contract with a GAP feature may do so through nonexclusive agents such as automobile dealers.

AUTH: 32-1-218, MCA; Sec. 1, Ch. 138, L. 2011

IMP: 32-1-429, MCA; Sec. 1, Ch. 138, L. 2011

STATEMENT OF REASONABLE NECESSITY: This rule pertaining to Guaranteed Asset Protection features of debt cancellation contracts derives from OCC Interpretative Letters #1028 and #1032 addressing whether GAP features are debt cancellation products, whether they run afoul of the anti-tying provision in NEW RULE IV(1)(a), and whether they may be offered through nonexclusive agents such as automobile dealers. Based on the numbers and types of inquiries from national banks to the OCC about GAP features of debt cancellation contracts, the

department believes that in the absence of this rule, there would likely be confusion about such matters among banks. The department believes this rule is necessary to clarify that potential area of confusion.

5. Concerned persons may present their data, views, or arguments concerning the proposed action to Lorraine Schneider, Legal Counsel, Division of Banking and Financial Institutions, P.O. Box 200546, Helena, Montana 59620-0546; faxed to the office at (406) 841-2930; or e-mailed to lschneider@mt.gov; and must be received no later than 5:00 p.m., September 8, 2011.

6. Lorraine Schneider, Department of Administration, has been designated to preside over and conduct this hearing.

7. The Division of Banking and Financial Institutions maintains a list of interested persons who wish to receive notices of rulemaking actions proposed by this division. Persons who wish to have their name added to the mailing list shall make a written request which includes the name and mailing address or e-mail address of the person to receive notices and specifies that the person wishes to receive notices regarding division rulemaking actions. Notices will be sent by e-mail unless a mailing preference is noted in the request. Such written requests may be mailed or delivered to Wayne Johnston, Division of Banking and Financial Institutions, 301 S. Park, Ste. 316, P.O. Box 200546, Helena, Montana 59620-0546; faxed to the office at (406) 841-2930; e-mailed to wjohnston@mt.gov; or may be made by completing a request form at any rules hearing held by the department.

8. An electronic copy of this Proposal Notice is available through the department's web site at <http://doa.mt.gov/administrativerules.mcp>. The department strives to make the electronic copy of the notice conform to the official version of the notice, as printed in the Montana Administrative Register, but advises all concerned persons that if a discrepancy exists between the official printed text of the notice and the electronic version of the notice, only the official printed text will be considered. In addition, although the department works to keep its web site accessible at all times, concerned persons should be aware that the web site may be unavailable during some periods, due to system maintenance or technical problems.

9. The bill sponsor contact requirements of 2-4-302, MCA, apply and have been fulfilled. On May 19, 2011, Rep. Tom Berry, primary bill sponsor of HB 432, was sent a letter with enclosed draft rules to the address on file for him with the Secretary of State. No comments were received.

By: /s/ Janet R. Kelly
Janet R. Kelly, Director
Department of Administration

By: /s/ Michael P. Manion
Michael P. Manion, Rule Reviewer
Department of Administration

Certified to the Secretary of State August 1, 2011.